



Improving Internal Controls-

A new model, framework, and tool-set to guide Management's evaluation process

A Presentation to:

**Designated Senior Officials and
Internal Auditors**

Date:

March 29, 2000

By:

**Office of Financial Management and
AuditForce, Inc.**



Introduction - Internal Controls

Presentation by:

Leon Hank



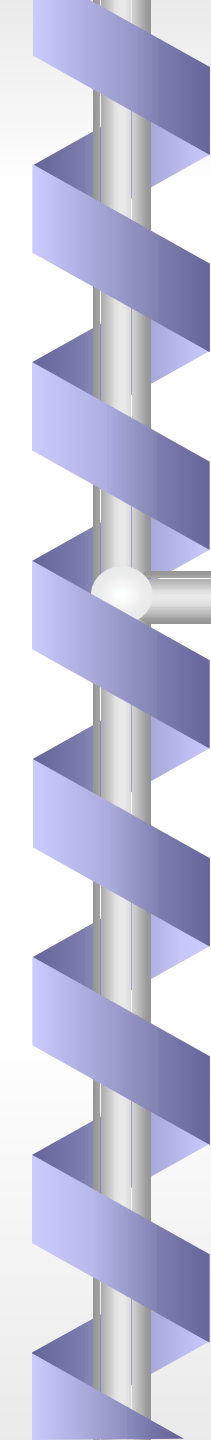
Overview of Today's Presentation

- ⌚ Introduction- Internal Controls
- ⌚ The new *General Framework* - why COSO?
(Steve Stier)
- ⌚ What is COSO?
(Cheryl McKellar - AuditForce, Inc.)
- ⌚ Luncheon video:
Controls in State government operations
- ⌚ The 2000 evaluation process - Issues
(Chris Bayley)
- ⌚ Round Table
(Leon Hank)



Introduction - Internal Controls

- ⌚ Internal Controls - What are they ???
- ⌚ Recent experiences demonstrating the importance of internal controls
- ⌚ Review of roles related to the internal control evaluation process



The New General Framework - why COSO-based ?

Presentation by:

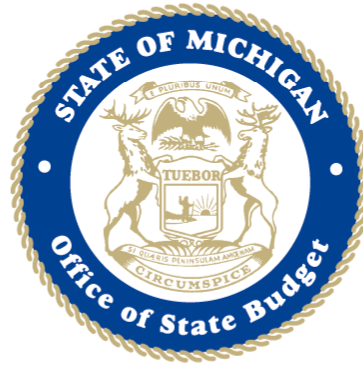
Steve Stier



Why the need for the new *General Framework* based on COSO?

- ⌚ Identifying issues related to the prior structure for evaluating controls
- ⌚ Review of developments in internal control literature
- ⌚ Benefits of building upon a widely-accepted model
- ⌚ Evaluation of Internal Controls -
A General Framework and System of Reporting

STATE OF MICHIGAN



EVALUATION OF INTERNAL CONTROLS

A GENERAL FRAMEWORK AND SYSTEM OF REPORTING

ISSUED BY THE
OFFICE OF FINANCIAL MANAGEMENT

1999 REVISION



What is COSO ?

Presentation by:

Cheryl McKellar

AUDITFORCE[®]
.....

Presentation Outline

- ⌚ History and Purpose of COSO
- ⌚ Internal Control Defined
- ⌚ Internal Control Objectives
- ⌚ COSO Components
- ⌚ Benefits
- ⌚ Management and IA Role
- ⌚ Tools





COSO

Committee of **S**ponsoring **O**rganizations



The Committee of Sponsoring Organizations of the Treadway Commission





COSO History - The Treadway Commission

- ⌚ Several business and alleged audit failures in the 1980's prompted creation of the Treadway Commission
- ⌚ Joint sponsorship by AICPA, AAA, FEI, IIA, and IMA
- ⌚ Examined causes of fraudulent financial reporting
- ⌚ Recommended forming COSO

COSO Purpose

- ∞ Determine a *common* definition for internal control and provide guidance for judging its effectiveness
- ∞ Develop integrated framework
- ∞ Create a control model

“Although there are several control models available, we believe that the most effective internal control guidance available today remains Internal Control - Integrated Framework published in 1992 by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).”

*John J. Fernandes, CIA, CCSA, IIA Chief Operating Officer
and Audit Committee Chairman for Bon Secours Health Systems*

Internal Control Defined

⌚ According to the **COSO**, internal control.....

- is a process. It is a means to an end, not an end in itself.
- is affected by people at every level of the organization.
- cannot be expected to provide more than reasonable assurance.
- is geared to the achievement of the entity's objectives in all areas, not just financial reporting.
- consists of interrelated components.



Internal Control Objectives

- ⌚ Safeguarding assets
- ⌚ Ensuring the accuracy and reliability of accounting data
- ⌚ Promoting operational efficiencies
- ⌚ Encouraging adherence to prescribed managerial policies



Components

- ∩ Control Environment
- ∩ Risk Assessment
- ∩ Control Activities
- ∩ Information and Communication
- ∩ Monitoring

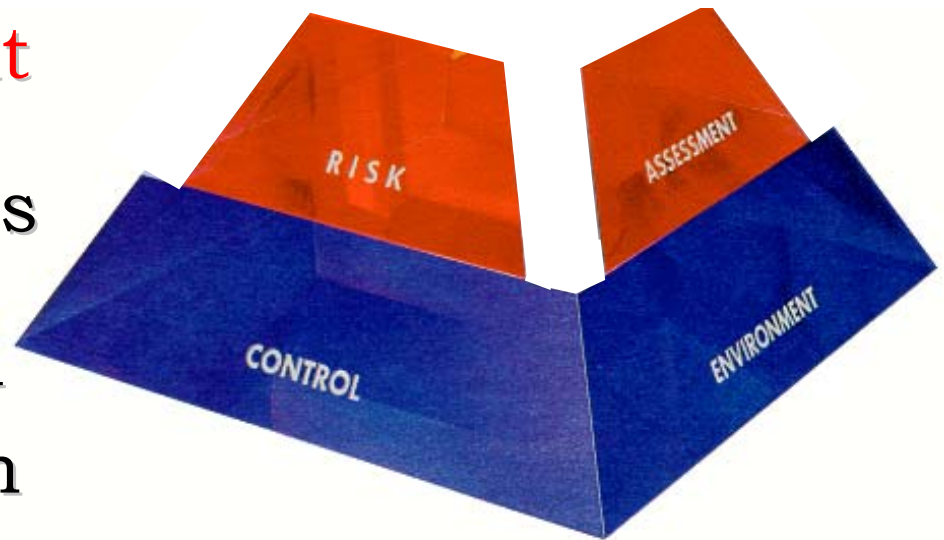
Components

- ∩ Control Environment
- ∩ Risk Assessment
- ∩ Control Activities
- ∩ Information and Communication
- ∩ Monitoring



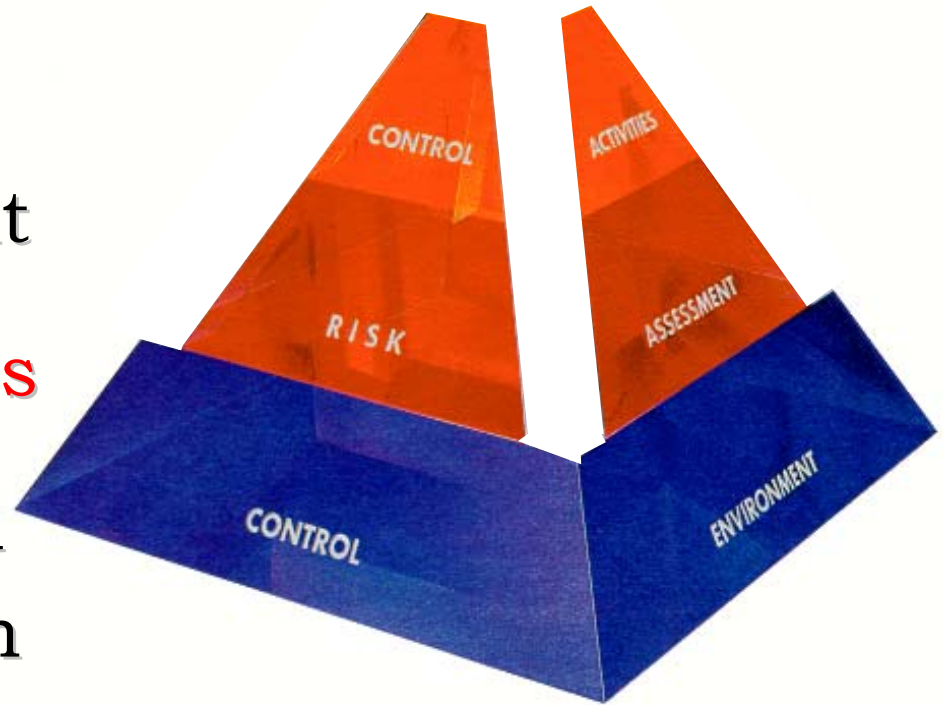
Components

- Control Environment
- Risk Assessment**
- Control Activities
- Information and Communication
- Monitoring



Components

- Control Environment
- Risk Assessment
- Control Activities**
- Information and Communication
- Monitoring



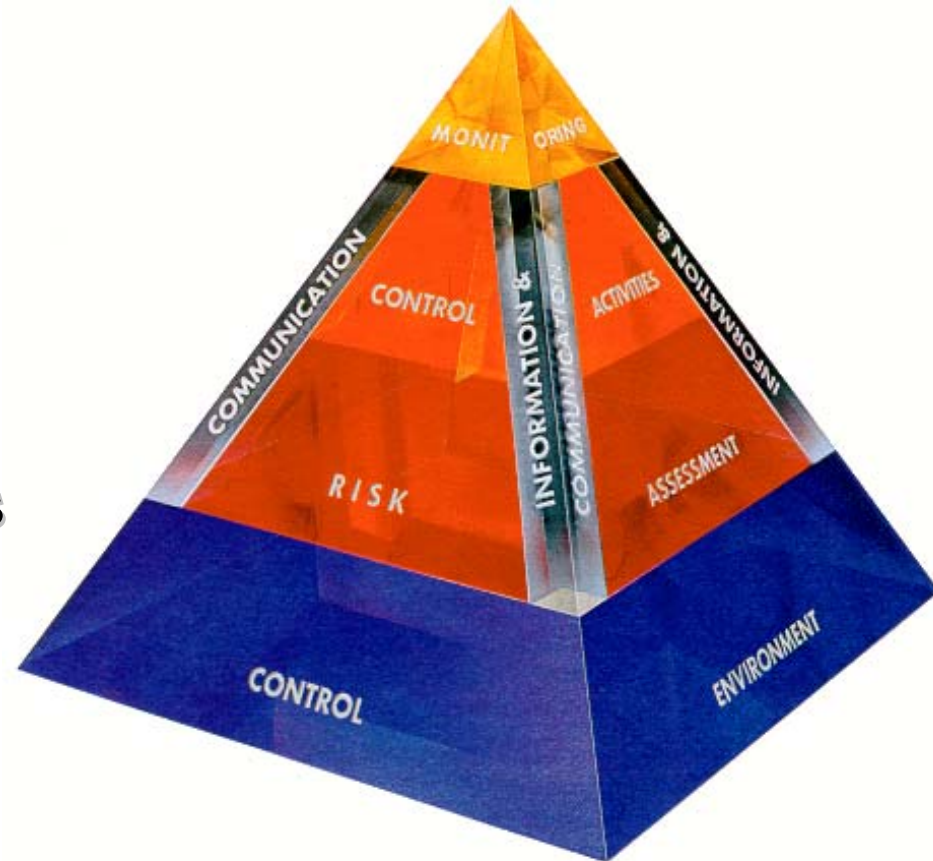
Components

- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication**
- Monitoring



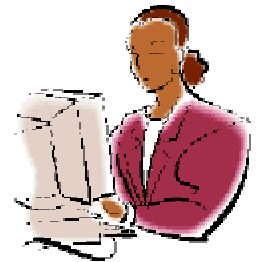
Components

- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication
- Monitoring



Responsibility

⌚ **Everyone** in an organization has responsibility for internal control.





Benefits to Management

- ∩ Deters inappropriate activity and loss of resources
- ∩ Minimizes surprises
- ∩ Is proactive
- ∩ Ties into quality initiatives

Benefits to Management (cont.)

- ⌚ Accurate financial and management reports, ensuring reliable information for making management decisions
- ⌚ Compliance with laws and regulations.
- ⌚ Assesses control systems against best practices



Benefits to Management (cont.)

- ∩ Common language
- ∩ Effective communication
- ∩ Enforces ethical values
- ∩ Adapts to management's philosophy and operating style
- ∩ Works across organizational lines



Benefits to Management (cont.)

- ⌚ Understanding the management of risk
- ⌚ Aids in achieving performance targets
- ⌚ Internal control is integrated into everyone's job responsibilities



Management's Responsibilities

- ⌚ Highly visible - Tone at the Top
- ⌚ Take ownership
- ⌚ Provide leadership and direction to management team
- ⌚ Drive control activities across organizational lines

Management's Role

- ⌚ Development of objectives and strategies
- ⌚ Analysis of risks
- ⌚ Development of policies and procedures to address risks



Management's Role (cont.)

- ❧ Implementing control activities to ensure actions are carried out
- ❧ Actively assist in monitoring and enhancing the system of control





Internal Auditor's Role

- ∩ Independently evaluate the effectiveness of components of the control system
- ∩ Partner with management to:
 - build assessment tools
 - assist in monitoring the control system
- ∩ Training, guidance, and consulting on internal control issues

Internal Auditor's Role (cont.)



When working in partnership with management, internal auditing can contribute positive, productive ideas about how opportunities and risks can be balanced and can make valuable recommendations for assessing and strengthening corporate governance.



*Anthony J. Ridley, CIA
General Auditor
Ford Motor Company*



Management Tools

- COSO Control Model

Can be tailored to an organization's structure and needs

Risk Assessment

+

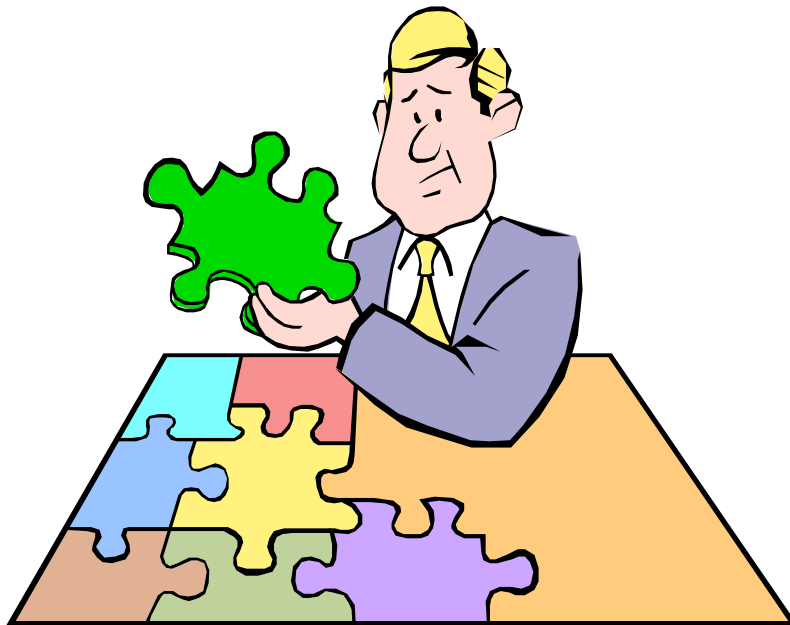
Self Assessment

=

Risk Assessment
and Control Activities
Worksheets

Integration Tools

“How to make it Simple”



- ⌚ Tone at the top
- ⌚ Organizational structure
- ⌚ Job descriptions
- ⌚ Policies and procedures
- ⌚ Training
- ⌚ Hiring practices



Successes Elsewhere

*Benchmarking statistics from Global Auditing Information Network (GAIN) found audit directors of 11 "world-class" audit departments ranked **partnering** and **risk management** as their best practices. The companies surveyed were DuPont, Carolina Power & Light, Ford Motor Company, Ameritech, IBM, Exxon, Southern California Edison, JC Penney, Microsoft, Asea Brown Boveri, and Motorola*



Summary

- ⌚ Management has a significant role in maintaining a sound internal control environment
- ⌚ COSO can provide effective, consistent, and comprehensive internal controls throughout State departments

Questions?





Thank you!!



Lunch/video

From the State of New York

**A WINNING STRATEGY:
Get Results with Internal Controls**



The 2000 Evaluation Process - Issues

Presentation by:

Chris Bayley



The 2000 Evaluation Process - Issues

Outline

- **Ongoing implementation approach**
- **DSO responsibilities**
- **Internal auditor responsibilities**
- **Management evaluation tool sets**
- **Reporting responsibilities**



The 2000 Evaluation Process - Issues

⌚ **On-going Implementation Approach**

- Top-level support
- Monitoring alternatives
- Other quality initiatives
- Training opportunities
- OFM will consult (upon request)



The 2000 Evaluation Process - Issues

⌚ **DSO Responsibilities**

- Segment the department
- Train activity-level managers
- Consolidate evaluation of activity-level assessments
- Draw overall conclusions



The 2000 Evaluation Process - Issues

⌚ **Internal Auditor Responsibilities**

- Monitor components of the internal control system
- Independently evaluate the effectiveness of components of the control system
- Partner with management
- Training, guidance, and consulting



The 2000 Evaluation Process - Issues

⌚ **Management Evaluation Tool Sets**

- Tools on the OFM website
- OFM's continuing research
- Encourage research by State departments



Office Responsibilities

Organization

Financial Reporting

Policies & Procedures

[User Guides](#)

[Letters/Directives](#)

Contact Us

FAQ

What's New

Related Links

State Phone Directory

State Email Directory

Evaluation Tool Sets

NOTE: Users wishing to download and customize the Word95/6.0 files can do so in one of the following ways.

PC Users: press the right mouse button on the link and select "Save Target As..."

Mac Users: press and hold mouse button on the link and select "Save Target As..."

[Background and Instructions for use of Evaluation Worksheets](#)

Control Environment - Evaluation Worksheet

[PDF](#)

[Word 95/6.0](#)

Information & Communication - Evaluation Worksheet

[PDF](#)

[Word 95/6.0](#)

**Risks, Control Activities, and Monitoring
(Non-Financial Activities) -Evaluation Worksheet**

[PDF](#)

[Word 95/6.0](#)

**Risks, Control Activities, and Monitoring Associated with
Financial Management Activities
- Evaluation Worksheet**

[PDF](#)

[Word 95/6.0](#)

**Internal Controls over Automated Information Systems -
Evaluation Worksheet**

[PDF](#)

[Word 95/6.0](#)

CobiT - Control Objectives

[PDF](#)

[Word 95/6.0](#)



The 2000 Evaluation Process - Issues

⌚ **Internal Auditor Tool**

- A number of factors were making the internal auditor job more challenging
 - Including numerous supporting information systems

The Solution!!

A new tool to enhance the State's internal auditor's monitoring capabilities



The 2000 Evaluation Process - Issues

OFFICE of FINANCIAL MANAGEMENT

AACE

Audit & Analysis
COMPUTER ENVIRONMENT



The 2000 Evaluation Process - Issues

⌚ **Reporting Responsibilities**

- New due date for report - May 1, 2001



Questions?



Round Table

Facilitator:

Leon Hank



Control weaknesses - war stories

- ⌚ Either move to front of presentation or delete